

Message Text

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ACTION NEA-12

INFO OCT-01 ISO-00 SPC-03 AID-20 EB-11 NSC-10 RSC-01

CIEP-02 TRSE-00 SS-20 STR-08 OMB-01 CEA-02 CIAE-00

COME-00 FRB-02 INR-10 NSAE-00 XMB-07 OPIC-12 LAB-06

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FM AMCONSUL KARACHI

TO AMEMBASSY ISLAMABAD

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TAGS: EFIN, PK

SUBJECT: NEW DOMESTIC RESERVE REQUIREMENT FOR
FOREIGN BANK BRANCHES

1. DELEGATION COMPRISED HEADS THREE AMERICAN BANKS
WITH BRANCHES IN PAKISTAN (FNCB, AMEX AND BANK OF AMERICA)
CALLED ON ME NOVEMBER 16 IN ORDER GIVE PRELIMINARY BRIEFING
CONCERNING THEIR INTENTION MADE PROTEST TO GOP NEXT FEW DAYS
CONCERNING PROJECTED CHANGE IN BANKING COMPANIES RULES OF 1963
WHICH WOULD REVOKE PRESENT EXCEPTION CONTAINED RULE 5 ON DEPOSITS,
WHICH ALLOWS FOREIGN BANKS TO MAINTAIN REQUIRED PAID-UP CAPITAL
(5 PERCENT OF TOTAL DEMAND AND TIME LIABILITIES) OUTSIDE
PAKISTAN IN SECURITIES AT NATIONAL BANK PAKISTAN BRANCH IN NEW
YORK FOR ACCOUNT OF STATE BANK. NEW DRAFT RULE, WHICH APPEARS
IN EXTRAORDINARY GAZETTE OF MAY 31, 1973 PAGE 857, SPECIFIES
PAID-UP CAPITAL AND RESERVES MUST NOW BE HELD IN PAKISTAN IN FORM
OF CASH OR "APPROVED (NON-FOREIGN) SECURITIES" TO BE DEPOSITED
"IN SUITABLE INSTALMENTS WHICH SHALL NOT EXTEND BEYOND 31 DECEMBER
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1977."

2. ALTHOUGH GAZETTE WAS DATED MAY 31, BANKERS DELEGATION SAID IT WAS NOT ACTUALLY CIRCULATED UNTIL JULY AND ALL U.S. BANK BRANCHES NOT AWARE ITS EXISTENCE OR SIGNIFICANCE UNTIL LAST WEEK. RULE CHANGE WOULD HAVE EFFECT OF FORCING ALL U.S. BANK BRANCHES HERE TO RETAIN PROFITS WITHIN PAKISTAN FOR NEXT FOUR OR FIVE YEARS OR OF REQUIRING IMPORT LARGE SUMS FOREIGN EXCHANGE TO COMPLY WITH DEPOSIT REQUIREMENT. IN CASE OF FNCB AMOUNT TO BE RETAINED IN COUNTRY FROM PROFITS, BASED ON

PRESENT LIABILITIES WOULD BE ABOUT \$2 MILLION, BUT COULD EXPAND WITH GROWING DEPOSITS TO AS MUCH AS \$4 MILLION BY 1977. BANK OF AMERICA MANAGER SAID AMOUNT FOR HIS BANK WOULD BE APPROXIMATELY SAME, WHILE AMEX WOULD HAVE TO IMPORT OR RETAIN ABOUT \$1.5 MILLION.

3. ALL BANK MANAGERS AGREED THAT NEW RULE IF IMPLEMENTED WOULD CONSTITUTE MOST SERIOUS STEP AGAINST FOREIGN BANKS WHICH COULD BE TAKEN BY STATE BANK SHORT OF OUTRIGHT NATIONALIZATION. THEY PARTICULARLY OBJECTED TO "OPEN EOR" CHARACTER OF NEW DOMESTIC RESEGHE REQUIREMENT, WHICH WOULD INCREASE WITH DEPOSITS, AND TO INDEFINITE SCHEDULE FOR PAYMENT. BANKERS OBSERVED THAT IF DOMESTIC DEPOSIT REQUIREMENT HAD BEEN CLEARLY STATED IN BANKING REGULATIONS BEFORE ESTABLISHMENT LOCAL BRANCH, THEN HEAD OFFICES COULD HAVE STUDIED RULES AND MADE DECISION ON WHETHER ENTER PAKISTAN ACCORDINGLY. IN THIS CASE, HOWEVER, STATE BANK NOW CONSIDERING CHANGING RULES "IN MID-STREAM" AFTER BRANCHES ESTABLISHED ON BASIS PREVIOUS CRITERIA. BANKERS ALSO FEARED "RIPPLE EFFECT" FROM DOMESTIC RESERVE REQUIREMENT WHICH COULD BE USED AS PRECEDENT AGAINST THEM IN OTHER DEVELOPING COUNTRIES INCLUDING INDIA.

4. U.S. BANK DELEGATION, PARTICULARLY FNCB, STRESSED ADVANTAGES WHICH GOP NOW ENJOYED FROM U.S. BRANCHES HERE THROUGH WHICH GOP ABLE OBTAIN SPECIAL FINANCING ARRANGEMENTS WHICH WOULD OTHERWISE NOT BE AVAILABLE. FNCB VICE PRESIDENT MENTIONED PARTICULARLY RECENT DC-76 AIRCRAFT FINANCING FOR PIA IN WHICH FNCB, AFTER EXIM BANK HESITANCY, HAD PROVIDED MAIN PART FINANCING AND THEREBY PERSUADED EXIM ALSO EXTEND CREDIT. FNCB EXPOSURE IN PAKISTAN HAD RISEN IN LAST YEAR TO \$100 MILLION INCLUDING \$45 MILLION TO PIA FROM ONLY \$35 MILLION A COUPLE OF YEARS AGO. THIS LIBERAL POLICY WOULD NEVER HAVE BEEN POSSIBLE IF BRANCHES FORCED TO HOLD 5 PER LIMITED OFFICIAL USE

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CENT RESERVES IN LOW PAYING PAKISTANI PAPER, WHICH HARDLY MOST FAVORED ASSET IN INTERNATIONAL BANKING WORLD.

5. MANAGERS ALL FOREIGN BANKS IN PAKISTAN INTEND TAKE PART IN DELEGATION WHICH WILL CALL ON FINANCE SECRDMARY A.G.N. KAZI AS SOON AS APPOINTMENT CAN BE ARRANGED. BANKERS HOPING FOR EXTENSION OF PERIOD FOR CONSIDERATION CHANGE IN BANKING RULES FROM PRESENT DEADLINE OF DECEMBER 1, 1973 IN ORDER MARSHAL STRONGEST ARGUMENT

AGAINST IMPLEMENTATION AND HOPEFULLY TO OBTAIN INDEFINITE POST-PONEMENT ANY CHANGE IN DOMESTIC CAPITAL REQUIREMENT.

6. COMMENT: DOMESTIC CAPITAL REQUIREMENT WAS FIRST BROUGHT UP IN 1970-71 WHEN FOREIGN BANKS SUCCESSFUL IN PUTTING OFF FURTHER CONSIDERATION OF MATTER. PRESENT RECONSIDERATION MAY AT BEST BE SIMPLE CONTINUATION OF PREVIOUS BUREAUCRATIC MOTION WHICH MAY AGAIN BE HEADED OFF IF GOP AT POLITICAL LEVEL REALIZES ADVERSE EFFECT ON OBTAINING NEW CREDITS THROUGH FOREIGN BANKS OUTWEIGHS ADVANTAGE OF GREATER MEASURE CONTROL WHICH STATE BANK WOULD ENJOY THROUGH IN-COUNTRY DEPOSIT 5 PER CENT FOREIGN BRANCH RESERVES. WE DO NOT SEE PRESENT MOVE, HOWEVER, AS CONNECTED WITH ANY PLANS FOR NATIONALIZATION SCHEDULED BANKS WHICH SOME RUMORS HERE FORESEE AS TAKING PLACE SOMETIME AFTER NEXT ELECTION.
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